



**STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY**



**LOCAL GOVERNMENT GROUP INSURANCE FUND**

**Financial and Compliance Audit Report**

For the Year Ended June 30, 2016

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**Justin P. Wilson, Comptroller**



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STATE OF TENNESSEE  
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January 20, 2017

The Honorable Bill Haslam, Governor  
Members of the General Assembly  
The Honorable Larry B. Martin, Chairman  
Local Government Insurance Committee

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Local Government Group Insurance Fund for the year ended June 30, 2016. You will note from the independent auditor's report that an unmodified opinion was given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance resulted in no audit findings.

Sincerely,

Deborah V. Loveless, CPA  
Director

**Audit Report**  
**Local Government Group Insurance Fund**  
**For the Year Ended June 30, 2016**

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State of Tennessee

# **A u d i t   H i g h l i g h t s**

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit

## **Local Government Group Insurance Fund**

For the Year Ended June 30, 2016

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### **Opinion on the Financial Statements**

The opinion on the financial statements is unmodified.

### **Audit Findings**

The audit report contains no findings.



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## **Independent Auditor's Report**

The Honorable Bill Haslam, Governor  
Members of the General Assembly  
The Honorable Larry B. Martin, Chairman  
Local Government Insurance Committee

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Local Government Group Insurance Fund, an enterprise fund of the State of Tennessee, as of and for the years ended June 30, 2016, and June 30, 2015, and the related notes to the financial statements, which collectively comprise the fund's basic financial statements as listed in the table of contents.

#### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

#### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting principles used and reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of directors of the Local Government Insurance Committee. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Local Government Group Insurance Fund.

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Local Government Group Insurance Fund of the State of Tennessee as of June 30, 2016, and June 30, 2015, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Emphasis of Matter***

As discussed in Note 1, the financial statements present only the Local Government Group Insurance Fund, an enterprise fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee, as of June 30, 2016, and June 30, 2015, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

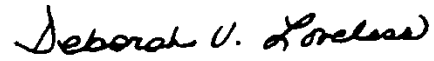
### ***Other Matter - Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the ten-year claims development information on pages 11 through 12 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### ***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated January 5, 2017, on our consideration of the fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations and contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an

integral part of an audit performed in accordance with *Government Auditing Standards* in considering the fund's internal control over financial reporting and compliance.

A handwritten signature in black ink, reading "Deborah V. Loveless". The signature is written in a cursive style with a large, stylized 'D' and 'L'.

Deborah V. Loveless, CPA

Director

January 5, 2017



**LOCAL GOVERNMENT GROUP INSURANCE FUND**  
**Statements of Net Position**  
**June 30, 2016, and June 30, 2015**

(Expressed in Thousands)

	<u>June 30, 2016</u>	<u>June 30, 2015</u>
<b>Assets</b>		
Current assets:		
Cash (Note 2)	\$43,794	\$40,446
Accounts receivable	1,863	874
<b>Total assets</b>	<b>45,657</b>	<b>41,320</b>
<b>Liabilities</b>		
Current liabilities:		
Accounts payable and accruals (Note 3)	6,701	6,502
Unearned revenue	37	28
<b>Total liabilities</b>	<b>6,738</b>	<b>6,530</b>
<b>Net position</b>		
Unrestricted	38,919	34,790
<b>Total net position</b>	<b>\$38,919</b>	<b>\$34,790</b>

The notes to the financial statements are an integral part of this statement.

**LOCAL GOVERNMENT GROUP INSURANCE FUND**  
**Statements of Revenues, Expenses, and Changes in Net Position**  
**For the Years Ended June 30, 2016, and June 30, 2015**

(Expressed in Thousands)

	<u>Year Ended June 30, 2016</u>	<u>Year Ended June 30, 2015</u>
<b>Operating revenues</b>		
Premiums	\$114,287	\$108,830
Total operating revenues	114,287	108,830
<b>Operating expenses</b>		
Contractual services	6,572	6,071
Benefits	102,326	95,261
Other	1,347	1,484
Total operating expenses	110,245	102,816
Total operating income	4,042	6,014
<b>Nonoperating revenues</b>		
Interest income	87	29
Total nonoperating revenues	87	29
Increase in net position	4,129	6,043
Net position - beginning of year	34,790	28,747
Net position - end of year	\$ 38,919	\$ 34,790

The notes to the financial statements are an integral part of this statement.

**LOCAL GOVERNMENT GROUP INSURANCE FUND**  
**Statements of Cash Flows**  
**For the Years Ended June 30, 2016, and June 30, 2015**

(Expressed in Thousands)

	Year Ended June 30, 2016	Year Ended June 30, 2015
<b>Cash flows from operating activities</b>		
Receipts from fund members	\$ 116,583	\$ 110,986
Payments to insurance companies and health care providers	(113,190)	(105,263)
Payments for state services	(132)	(100)
Net cash from operating activities	3,261	5,623
<b>Cash flows from investing activities</b>		
Interest received	87	29
Net cash from investing activities	87	29
Net increase in cash	3,348	5,652
Cash - beginning of the year	40,446	34,794
Cash - end of the year	\$ 43,794	\$ 40,446
<b>Reconciliation of operating income to net cash from operating activities</b>		
Operating income	\$ 4,042	\$ 6,014
Adjustments to reconcile operating income to net cash from operating activities:		
Changes in assets and liabilities:		
Change in accounts receivable	(989)	(166)
Change in accounts payable	199	(237)
Change in unearned revenue	9	12
Net cash from operating activities	\$ 3,261	\$ 5,623

The notes to the financial statements are an integral part of this statement.

**LOCAL GOVERNMENT GROUP INSURANCE FUND**  
**Notes to the Financial Statements**  
**June 30, 2016, and June 30, 2015**

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**Note 1. Summary of Significant Accounting Policies**

**Reporting Entity**

The Local Government Group Insurance Fund is used to account for revenues received and claims paid on behalf of current employees of local governments and quasi-governmental organizations established for the primary purpose of providing services for or on behalf of state and local governments. The fund has been included as an enterprise fund in the *Tennessee Comprehensive Annual Financial Report*. That report is available on the state's website at [www.tn.gov/finance/article/fa-accfin-cafr](http://www.tn.gov/finance/article/fa-accfin-cafr).

**Basis of Presentation**

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

**Measurement Focus and Basis of Accounting**

The accompanying financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Operating revenues and expenses are distinguished from nonoperating items in the Local Government Group Insurance Fund. Operating revenues and expenses generally result from providing services in connection with the fund's principal ongoing insurance operations. Operating expenses include the cost of those services and administrative expenses. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

**Cash**

Cash is defined as cash on hand and demand deposits, such as the pooled investment fund.

**Note 2. Deposits**

The Local Government Group Insurance Fund had \$43,794,059 and \$40,445,529 in the State Pooled Investment Fund (SPIF) at June 30, 2016, and June 30, 2015, respectively. The SPIF, administered by the State Treasurer, is authorized by statute to invest funds in accordance with policy guidelines approved by the State Funding Board. The current resolution of that board gives the Treasurer approval to invest in collateralized certificates of deposit in authorized state depositories; prime commercial paper; prime bankers' acceptances; bonds, notes, and bills of the United States Treasury or other obligations guaranteed as to principal and interest by the United

## Notes to the Financial Statements (Continued)

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States or any of its agencies; repurchase agreements for obligations of the United States or its agencies; and securities lending agreements whereby securities may be loaned for a fee.

There are no minimum or maximum limitations on withdrawals from the SPIF with the exception of a 24-hour notification period for withdrawals of \$5 million or more. Investments in the SPIF are measured at amortized cost. The pooled investment fund's required risks disclosures are presented in the *State of Tennessee Treasurer's Report*. That report is available on the state's website at [www.treasury.tn.gov](http://www.treasury.tn.gov) or by calling (615) 741-2956.

### Note 3. Risk Management

The Local Government Group Insurance Fund, a public entity risk pool, was established in July 1991 to provide a program of health insurance coverage for employees of local governments and quasi-governmental organizations that were established for the primary purpose of providing services for or on the behalf of state and local governments. In accordance with Section 8-27-401, *Tennessee Code Annotated*, all local governments and quasi-governmental organizations described above are eligible to participate. Fund members at June 30, 2016, included 66 counties, 152 municipalities, and 135 quasi-governmental organizations, with 14,059 active employees maintaining coverage through one of four options: partnership preferred provider organization (PPO) plan, standard PPO plan, PPO limited plan, or the healthsavings consumer driven health plan (CDHP). The state does not retain any risk for losses by this fund.

The Local Government Group Insurance Fund assumes responsibility for determining plan benefits and eligibility, establishing premiums sufficient to fund plan obligations, recording and reporting financial transactions accurately, reporting enrollment to vendors, processing claims submitted for services provided to plan participants, communicating with plan participants, and complying with appropriate state and federal laws and regulations. Plan participants are required to pay premiums on time, file claims for services received, report changes in eligibility of themselves or their dependents, and ensure that only eligible expenses are paid by the plan. Individuals who cancel coverage may be required to demonstrate a qualifying event to rejoin the plan. Employers must wait 24 months before rejoining the plan if the employer elects to withdraw from the plan.

The Local Government Group Insurance Fund establishes claims liabilities for self-insured options based on estimates of the ultimate cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims. The process used to compute claims liabilities does not necessarily result in an exact amount. Claims liabilities are recomputed periodically using actuarial and statistical techniques to produce current estimates. Adjustments to claims liabilities are charged or credited to expense in the period in which they are made. The Local Government Group Insurance Fund considers investment income in determining if a premium deficiency exists.

## Notes to the Financial Statements (Continued)

As discussed above, the Local Government Group Insurance Fund establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities during the past two years (expressed in thousands):

	<u>2016</u>	<u>2015</u>
Unpaid claims at the beginning of the year	\$ 5,765	\$ 6,032
Incurred claims:		
Provision for insured events of the current year	109,589	100,806
Decrease in provision for insured events of prior years	(1,062)	(224)
<u>Total incurred claims expenses</u>	<u>108,527</u>	<u>100,582</u>
Payments:		
Claims attributable to insured events of the current year	103,637	95,096
Claims attributable to insured events of prior years	4,702	5,753
<u>Total payments</u>	<u>108,339</u>	<u>100,849</u>
<u>Total unpaid claims at the end of the year</u>	<u>\$ 5,953</u>	<u>\$ 5,765</u>

**LOCAL GOVERNMENT GROUP INSURANCE FUND**  
**Required Supplementary Information**  
**Ten-Year Claims Development Information**

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The table below illustrates how the Local Government Group Insurance Fund's earned revenues and investment income compare to related costs of loss and other expenses assumed by the fund for each of the last ten years. The rows of the table are defined as follows: (1) This line shows the total of each fiscal year's earned contribution revenues and investment revenues. (2) This line shows each fiscal year's other operating costs of the fund, including overhead and claims expense not allocable to individual claims. (3) This line shows the fund's incurred claims and allocated claim adjustment expenses (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called policy year); some of these amounts are unavailable. (4) This section shows the cumulative amounts paid as of the end of successive years for each policy year; some of these amounts are unavailable. (5) This section shows how each policy year's incurred claims increased or decreased as of the end of successive years; some of these amounts are unavailable. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known. (6) This line compares the latest reestimated incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of claims cost is greater or less than originally thought. As data for individual policy years mature, the correlation between original estimates and reestimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature fiscal years. The columns of the table show data for successive fiscal and policy years.

**Fiscal and Policy Year Ended**  
**(expressed in thousands of dollars)**

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>
(1) Required contribution and investment revenue earned (fiscal year)	\$89,240	\$96,558	\$103,157	\$104,810	\$102,710
(2) Unallocated expenses (fiscal year)	3,398	3,500	4,348	5,921	5,473
(3) Estimated incurred claims and expenses, end of policy year	91,622	94,655	100,350	107,083	91,699
(4) Paid (cumulative) as of:					
End of policy year	84,836	88,265	93,456	98,709	89,231
One year later	91,791	94,820	100,916	105,833	91,703
Two years later	91,793	95,029	101,895	107,170	91,618
Three years later	93,594	94,993	100,533	107,103	91,578
Four years later	93,594	94,991	100,494	107,101	91,669
Five years later	93,591	94,991	100,494	107,101	*
Six years later	93,591	94,991	100,494	*	
Seven years later	93,591	94,991	*		
Eight years later	93,591	*			
Nine years later	*				

## Ten-Year Claims Development Information

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>
(5) Reestimated incurred claims and expenses:					
End of policy year	91,622	94,655	100,350	107,083	91,699
One year later	91,801	94,749	100,803	106,870	91,640
Two years later	91,788	94,999	101,895	106,720	91,558
Three years later	93,594	94,993	100,492	106,697	91,669
Four years later	93,594	94,993	100,492	106,697	91,669
Five years later	93,594	94,993	100,492	106,697	*
Six years later	93,594	94,993	100,492	*	
Seven years later	93,594	94,993	*		
Eight years later	93,594	*			
Nine years later	*				
(6) Increase (decrease) in estimated incurred claims and expenses from end of policy year	1,972	338	142	(386)	(30)

### Fiscal and Policy Year Ended (expressed in thousands of dollars)

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
(1) Required contribution and investment revenue earned (fiscal year)	\$103,278	\$105,973	\$108,834	\$108,860	\$114,373
(2) Unallocated expenses (fiscal year)	6,010	6,135	6,645	7,535	8,012
(3) Estimated incurred claims and expenses, end of policy year	94,738	96,152	99,097	103,694	*
(4) Paid (cumulative) as of:					
End of policy year	88,026	89,634	92,792	97,837	*
One year later	94,277	96,101	98,622	*	
Two years later	94,205	95,919	*		
Three years later	94,183	*			
Four years later	*				
(5) Reestimated incurred claims and expenses:					
End of policy year	94,738	96,152	99,097	103,694	*
One year later	94,248	96,022	98,653	*	
Two years later	94,192	95,895	*		
Three years later	94,182	*			
Four years later	*				
(6) Increase (decrease) in estimated incurred claims and expenses from end of policy year	(556)	(257)	(444)	0	*

\* Data not available.





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**Independent Auditor's Report on Internal Control Over  
Financial Reporting and on Compliance and Other Matters  
Based on an Audit of Financial Statements Performed in  
Accordance With *Government Auditing Standards***

The Honorable Bill Haslam, Governor  
Members of the General Assembly  
The Honorable Larry B. Martin, Chairman  
Local Government Insurance Committee

We have audited the financial statements of the Local Government Group Insurance Fund as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the fund's basic financial statements, and have issued our report thereon dated January 5, 2017. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Local Government Group Insurance Fund's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the fund's internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did

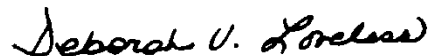
not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Local Government Group Insurance Fund's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Purpose of This Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Deborah V. Loveless, CPA  
Director  
January 5, 2017